INDEX

	Page
Opinion below	1
Jurisdiction	1
Question presented	2
Statutes involved	2
Statement	2
Specification of error	4
Summary of argument	4
Argument	7
I The case falls within the terms of Section 219 (g) of the Revenue Act of 1924	8
II To tax to the settlor the income of the trusts in question is not an unreasonable exercise of the taxing power	11
III The statute does not have an invalid retroactive operation	24
Conclusion	27
Appendix (statutes involved)	28–29

CITATIONS

Cases:	
Bing v. *Bowers*, 26 F. (2d) 1017	19
Blodgett v. *Holden*, 275 U. S. 142	25
Bromley v. *Commissioner*, 26 B. T. A. 878	23
Bromley v. *McCaughn*, 280 U. S. 124	5, 12
Brushaber v. *Union Pac. R. R. Co.*, 240 U. S. 1	26
Bullen v. *Wisconsin*, 240 U. S. 625	22
Burnet v. *Guggenheim*, No. 283, decided February 6, 1933	16, 21, 22, 23
Burnet v. *Leininger*, 285 U. S. 136	13, 19, 20
Chase National Bank v. *United States*, 278 U. S. 327	18
Cohan v. *Commissioner*, 39 F. (2d) 540	11
Commissioner v. *McCormick*, 43 (2d) 277, reversed, 284 U. S. 784	14
Corliss v. *Bowers*, 281 U. S. 376	5, 7, 12, 13, 14, 15, 26
Corliss v. *Bowers*, 34 F. (2d) 656, aff'd, 281 U. S. 376	23
Dickey v. *Burnet*, 56 F. (2d) 917, certiorari denied October 10, 1932	19, 22
Farmers' Loan & Trust Co. v. *Bowers*, 29 F. (2d) 14	18
Fawcus Machine Co. v. *United States*, 282 U. S. 375	25
Gwinn v. *Burnet*, No. 31, decided December 5, 1932	18

Cases—Continued. Page

Hoeper v. *Wisconsin*, 284 U. S. 206 ..... 6, 21, 22
Larkin v. *Wikoff*, 75 N. S. Eq. 462 9
Leydig v. *Commissioner*, 43 F. (2d) 494 19
Lucas v. *Earl*, 281 U. S. 111 ..... 13, 19
Lynch v. *Hornby*, 247 U. S. 339 26
McCauley v. *Commissioner*, 44 F. (2d) 919 22
Massachusetts Mutual Life Ins. Co. v. *United States*, No. 322, decided February 6, 1933 11
Mitchel v. *Bowers*, 15 F. (2d) 287, certiorari denied, 273 U. S. 759 19
Moyer v. *Peabody*, 212 U. S. 78 11
Nashville, Chattanooga, & St. Louis Railway v. *Wallace*, No. 176, decided February 6, 1933 ..... 5, 12
Nelson v. *Ferguson*, 56 F. (2d) 121, certiorari denied, 286 U. S. 565 19
Nichols v. *Coolidge*, 274 U. S. 531 ..... 7, 25
Old Colony R. Co. v. *Commissioner*, 284 U. S. 552 10
Parker v. *Routzahn*, 56 F. (2d) 730 19
Philips v. *Dime Safe D. & T. Co.*, 284 U. S. 160 18
Porter v. *Commissioner*, 60 F. (2d) 673, No. 466, Oct. Term, 1932 ..... 17, 22
Porter v. *United States*, 52 F. (2d) 1056 19
Reinecke v. *Northern Trust Co.*, 278 U. S. 339 ..... 12, 18
Saltonstall v. *Saltonstall*, 276 U. S. 260 ..... 5, 6, 12, 16, 18
Smith v. *Commissioner*, 23 B. T. A. 631, reversed, 59 F. (2d) 56 9
Stewart v. *Commissioner*, B. T. A., decided January 31, 1933 18
Third National Bank & Trust Co. v. *White*, No. 202, decided December 19, 1932 18
Title Guarantee Loan & Trust Co. v. *Commissioner*, C. C. A. 5th, decided February 17, 1933 .....
Tyler v. *United States*, 281 U. S. 497 ..... 6, 11, 17, 18, 21
United States v. *Cooper*, 280 U. S. 409 25
Untermyer v. *Anderson*, 276 U. S. 440 ..... 7, 25
Van Meter v. *Commissioner*, 61 F. (2d) 817 19
Ward v. *Commissioner*, 58 F. (2d) 757 19
Weiss v. *Stearn*, 265 U. S. 242 21
Wells v. *Commissioner*, C. C. A. 8th, decided February 4, 1933 16
White v. *Erskine*, 47 F. (2d) 1014 18

Statutes:

Revenue Act of 1924, c. 234, 43 Stat. 253, 267, 275, 304—
Sec. 213 (U. S. C., Title 26, Sec. 954) 23
Sec. 219 (U. S. C., Title 26, Sec. 960) 28
Sec. 283 28
Sec. 302 (U. S. C., Title 26, Sec. 1094) 29
Revenue Act of 1926, c. 27, 44 Stat. 9, 32—
Sec. 219 (U. S. C. App., Title 26, Sec. 960) 10

Statutes—Continued. Page

Revenue Act of 1928, c. 852, 45 Stat. 791, 840—
Sec. 166 (U. S. C. Sup. V, Title 26, Sec. 2166) 10
Revenue Act of 1932, c. 209, 47 Stat. 169, 221—
Sec. 166 (U. S. C. Sup. VI, Title 26, Sec. 166) 10

Miscellaneous:
American Law Institute, Restatement of Trusts, Section 122, Comment b 9
House Rep. No. 179, 68th Cong., 1st Sess., p. 21 23
I. T. 2145, IV–1 Cumulative Bulletin 43 23
Regulations 65, Article 347 10
Regulations 67, Article 1 23
Regulations 69, Article 347 10
Regulations 74, Article 881 10
Regulations 77, Article 881 10
Sen. Rep. No. 398, 68th Cong., 1st Sess., p. 25 ..... 20, 23

In the Supreme Court of the United States

OCTOBER TERM, 1932

No. 601

MABEL G. REINECKE, FORMERLY COLLECTOR OF INTERNAL REVENUE FOR THE FIRST DISTRICT OF ILLINOIS, petitioner

v.

KENNETH G. SMITH AND FOREMAN-STATE TRUST AND SAVINGS BANK, Executors of the Will of Douglas Smith

ON A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE PETITIONER

OPINION BELOW

The District Court filed no opinion. The opinion of the Circuit Court of Appeals (R. 95–97) is reported in 61 F. (2d) 324.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered October 7, 1932. (R. 97.) The petition for certiorari was filed January 7, 1933, and was granted February 13, 1933. (R. 99.) The

jurisdiction of this Court rests on Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION INVOLVED

Whether Section 219 (g) of the Revenue Act of 1924, which taxes the income of a trust to the grantor if during the taxable year he has the power, in conjunction with any person not a beneficiary, to revoke the trust, is constitutional as applied to trusts in which the grantor reserved the power to revoke with the consent of a trustee.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra*, pp. 28–29.

STATEMENT

This action was brought in the United States District Court for the Northern District of Illinois to recover income taxes asserted to have been exacted unlawfully of the respondents' testate, Douglas Smith, by the petitioner while Collector of Internal Revenue. The petitioner demurred to the complaint on the ground that the facts alleged did not constitute a cause of action. (R. 83.) The demurrer was overruled (R. 83) and upon the petitioner's refusal to plead over judgment was entered for the respondents (R. 84).

The complaint (R. 2–80) alleged that in 1922 the decedent created five trusts, one each for the benefit of his wife and three children and the fifth for the

joint benefit of all of them. The trustees were the same in all cases and consisted of the settlor, a trust company, and the decedent's son, who, in addition to being the immediate beneficiary in the trust set up for him, was a contingent beneficiary under the other trusts. Neither the settlor nor the trust company was a beneficiary under any of them.

Each trust instrument contained the following provision (R. 56, 61, 66, 71, 78):

> Anything herein contained to the contrary notwithstanding, this Trust may be modified or revoked at any time by an instrument in writing signed by Douglas Smith, and either one of the other two trustees or their successors.

Pursuant to this power each of the individual trusts was modified at least once, and in the case of the wife's trust by the insertion of a provision that the trust fund should be in lieu of the wife's dower and statutory interests in the grantor's estate. (R. 59, 64, 69, 74.) On October 22, 1924, the grantor resigned as trustee, and at that time all the trust instruments were again amended by the elimination of the power to modify or revoke. (R. 8.)

The settlor did not include any of the income of the five trusts in his income tax return for 1924. He was required by the petitioner, however, pursuant to the provisions of Section 219 (g) of the Revenue Act of 1924 (*infra*, p. 28), to file an amended return including such income up to October 22,

1924, and to pay a tax computed upon the aggregate income so returned. The settlor then filed a claim for refund of the additional tax paid by reason of the inclusion of the trust income in his return and upon its rejection brought this suit. (R. 9–11.)

Upon appeal to the Circuit Court of Appeals the judgment for the respondents was affirmed on the ground that as applied to the facts of this case Section 219 (g) was unconstitutional under the due process clause of the Fifth Amendment.

SPECIFICATION OF ERROR

The Circuit Court of Appeals erred in holding that Section 219 (g) of the Revenue Act of 1924 contravenes the Constitution when applied to a trust created in 1922, under which the grantor had the power in conjunction with a trustee to modify or revoke the trust.

SUMMARY OF ARGUMENT

I

The case falls within the terms of Section 219 (g) of the Revenue Act of 1924 (*infra*, p. 28). That section provides that the income of a trust shall be taxable to the settlor when he has the power to revoke the trust, either alone or in conjunction with any person not a beneficiary of the trust. In this case the trust could be terminated by the settlor and the corporate trustee acting jointly. The corporate trustee was not a beneficiary of the trust within the meaning of the statute.

II

Although the decedent's interest in the property was qualified, it was nevertheless substantial, and he was not a stranger to the title. His rights and interests were elements in the totality of rights and interests which made up complete ownership, and his retention of this interest was a sufficient basis for the imposition of the tax. *Nashville, Chattanooga & St. Louis Ry.* v. *Wallace,* No. 176, October Term, 1932, decided February 6, 1933; *Bromley* v. *McCaughn,* 280 U. S. 124, 136–138.

The fact that the right to revoke could be exercised only with the concurrence of a trustee does not distinguish this case from *Corliss* v. *Bowers,* 281 U. S. 376. *Saltonstall* v. *Saltonstall,* 276 U. S. 260, where the situation was precisely the same as that at bar, makes that clear. The power of revocation was subject to no fiduciary limitations, express or implied. When exercised with the consent of the trustee, who had no interest adverse to the settlor and was no doubt selected to do his will, it was as absolute as the power in *Corliss* v. *Bowers.*

Whether the settlor retains sufficient command of income to warrant his being taxed would seem to be less a problem of technicalities than of actualities. Where a settlor retains command over property, it is not unreasonable to suppose that nothing has been done in sharing such command which will defeat the settlor's purpose to exercise command.

The principle which should control decision in this case has been applied by this Court in cases involving estate and inheritance taxes. *Saltonstall* v. *Saltonstall*, 276 U. S. 260; *Tyler* v. *United States*, 281 U. S. 497. If, as these cases seem to show, it would have been neither arbitrary nor capricious for Congress to have included the corpus of the trusts in question in the grantor's estate had he died prior to October 22, 1924, it would seem equally clear that it is neither arbitrary nor capricious for Congress to impose upon the grantor during his life a tax based upon the income of these trusts.

A person may not escape liability for tax upon income by assigning it to another, unless he irrevocably and unqualifiedly gives him as well the property which produces it. The same result should be applied to a disposition of income through the device of a trust.

This case is not like *Hoeper* v. *Tax Commission*, 284 U. S. 206. There is no attempt here to tax one person for income derived by another from his own separate property. Here the beneficiaries had no power to pledge, sell, or bequeath the property. Only the grantor and one of the two trustees had power to exercise all the incidents of absolute ownership of the property. It lay in their power to control and dispose of the corpus without even consulting the beneficiaries.

III

The court below decided that the statute was unconstitutional when applied to the trusts involved in this case, since they were created in 1922 before the enactment of the Revenue Act of 1924. We submit that this position is without merit.

Cases like *Nichols* v. *Coolidge,* 274 U. S. 531, and *Untermyer* v. *Anderson,* 276 U. S. 440, turned upon the power of Congress to tax transfers or gifts made and completed before the laws assuming to tax them were enacted. Here the United States is not taxing the creation of the trusts or the transfer of the securities to the trustees, but the income received from the shares of stock after the effective date of the Revenue Act of 1924. Certainly there is no retroactivity as to the income rising after June 2, 1924, the date the Revenue Act of 1924 was enacted. And as to the income arising in 1924 before June 2, 1924, the case seems indistinguishable from *Corliss* v. *Bowers,* 281 U. S. 376, where the trust in question, like the trusts here in issue, was created in 1922. The statute was sustained although the taxpayer contended that it was invalid on account of retroactivity.

ARGUMENT

Section 219 (g) of the Revenue Act of 1924 provides:

> Where the grantor of a trust has, at any time during the taxable year, either alone or in conjunction with any person not a

> **beneficiary of the trust, the power to revest in himself title to any part of the corpus of the trust, then the income of such part of the trust for such taxable year shall be included in computing the net income of the grantor.**

In the present case the decedent was the creator of the trusts. He, a trust company, and his son were the trustees of the trusts. He and either one of the other two trustees had the power at any time to modify or revoke the trusts. The decedent's son was the principal beneficiary of one of the trusts, and a contingent beneficiary of the others; the trust company was not a beneficiary of any of the trusts.

On October 22, 1924, the decedent resigned as trustee, and with the consent of the other trustees the power to modify or revoke was eliminated. Only the income accruing to the trusts in 1924 prior to October 22, 1924, is involved in this case.

We contend that Section 219 (g) makes this income taxable to the creator of the trusts, and that the statute when so applied is constitutional.

I

THE CASE FALLS WITHIN THE TERMS OF SECTION 219 (g) OF THE REVENUE ACT OF 1924

The respondents contended before the courts below (R. 96) that the term "beneficiary" in Section 219 (g) of the Revenue Act of 1924 (*infra*, p. 28) includes a trustee and that for this reason

the case is without the statute. Whether the District Court reached its conclusion upon the basis of this argument does not appear, since it rendered no opinion. In the Circuit Court of Appeals the point was passed, the court being of opinion that in any event application of the statute to the present trusts is in violation of the Constitution.

We believe this preliminary contention of the taxpayers plainly without merit. The statute is clear, and excludes from its scope only powers of revocation exercisable by a grantor acting jointly with one or more beneficiaries. A trustee, whatever his duties in respect of the trust property, is not by virtue of his office alone a beneficiary.[1] The beneficiary is the person for whom property is held; the trustee is the person who holds it. *Larkin* v. *Wikoff*, 75 N. J. Eq. 462, 474. Cf. *Smith* v. *Commisioner*, 23 B. T. A. 631, reversed, 59 F. (2d) 56 (C. C. A. 1st); *Title Guarantee Loan & Trust Co.* v. *Commissioner*, decided February 17, 1933 (C. C. A. 5th). This is the commonly understood meaning of the term beneficiary, and it is not to be assumed that Congress used the word in any other

[1] In the American Law Institute's Restatement of Trusts, Section 122, Comment *b*, the rule is stated as follows: "Although a trustee is entitled to compensation for acting as trustee (see Section —), he is not as such a beneficiary of the trust."

The respondents themselves state that "Douglas Smith, the grantor, was not a beneficiary under any of the trusts." (Br. in Opp. 3.) Yet he was a trustee with exactly the same rights and powers as the trust company.

than its ordinary acceptation. *Old Colony R. Co.* v. *Commissioner,* 284 U. S. 552, 560. That this was in fact the intention of Congress is made abundantly clear when Section 219 is read in its entirety, for "fiduciary" and "beneficiary" are used throughout the section as words of contrast.

This is the view which the Treasury Department has adopted in administering the statute. Article 347 of Regulations 65, promulgated under the Revenue Act of 1924, provides among other things that—

> The term "beneficiary" as used in this article includes any person entitled to an interest in the income or the principal of a trust, but does not include one having merely a nominal interest in the income or principal.

This interpretation has been consistently applied under the corresponding provisions of the later Revenue Acts.[2] Regulations 69, Article 347, promulgated under the Revenue Act of 1926; Regulations 74, Article 881, promulgated under the Revenue Act of 1928. Under these circumstances, as this Court has many times held, the executive in-

[2] Section 219 (g) of the Revenue Act of 1926, c. 27, 44 Stat. 32 (U. S. C. App., Title 26, Sec. 960); Section 166 of the Revenue Act of 1928, c. 852, 45 Stat. 840 (U. S. C. Sup. V, Title 26, Sec. 2166). The provision is worded somewhat differently in Section 166 of the Revenue Act of 1932, c. 209, 47 Stat. 221 (U. S. C. Sup. VI, Title 26, Sec. 166). See Article 881 of Regulations 77 under the 1932 Act.

terpretation must be regarded as expressing the intent of Congress. *Massachusetts Mutual Life Ins. Co.* v. *United States,* No. 322, October Term, 1932, decided February 6, 1933.

The grantor and the trustee bank jointly had the power to alter or terminate the five trusts. The case is clearly within the terms of Section 219 (g), and no question of statutory construction is involved.

II

TO TAX TO THE SETTLOR THE INCOME OF THE TRUSTS IN QUESTION IS NOT AN UNREASONABLE EXERCISE OF THE TAXING POWER

The Fifth Amendment, upon which the respondents here rely, does not provide a rigid rule delimiting the power of Congress. It requires only that exercise of the taxing power must not be arbitrary or capricious—must not pass beyond the "admonitions of fair dealing." *Tyler* v. *United States,* 281 U. S. 497, 504; *Moyer* v. *Peabody,* 212 U. S. 78, 84; *Cohan* v. *Commissioner,* 39 F. (2d) 540, 545 (C. C. A. 2d). That, we believe, the tax in this case does not do.

It is plain that the decedent retained a substantial interest in the trust property. True, this interest was hedged in by the requirement that it could be enjoyed only with the consent of one of the two other trustees, but nevertheless the decedent's interest was far different from that of a stranger to the title and constituted a substantial interest in the trust property. This interest, though quali-

fied, was one of the totality of rights and interests which constituted complete ownership of the property. The propriety of the tax would therefore seem to be established by this Court's recent declaration that "The power to tax property * * * necessarily includes the power to tax its constituent elements." *Nashville, Chattanooga & St. Louis Railway* v. *Wallace*, No. 176, October Term, 1932, decided February 6, 1933. See also *Bromley* v. *McCaughn*, 280 U. S. 124, 136–138.

In *Corliss* v. *Bowers*, 281 U. S. 376, this Court held that it is not beyond the power of Congress to tax a person upon income given another through the device of a trust where the donor does not give the donee as well the property which produces that income but retains to himself alone the right to revest title to the property. The fact that the right to revoke here could be exercised only with the concurrence of another whom the settlor had chosen to act with him does not, we submit, serve as a sufficient basis to distinguish this case from *Corliss* v. *Bowers*. *Saltonstall* v. *Saltonstall*, 276 U. S. 260 (see p. 17, *infra*), where the situation was precisely the same as that at bar, makes that clear. Nor does it bring the case within the decision as to the "five trusts" involved in *Reinecke* v. *Northern Trust Co.*, 278 U. S. 339, since one of the trustees was not a beneficiary. Although a trustee owes fiduciary duties to the beneficiaries with respect to the administration of the trust and the preservation of the trust property, he obviously has no such

obligation with respect to such a power as that involved in this case. To imply a fiduciary limitation upon a power to revoke the trust would annihilate the power, because revocation terminates the trust and the interest of the beneficiary. The trustee, it is true, is under no legal duty to join with the settlor in revoking the trust, but having derived his power of revocation under the trust instrument executed by the settlor for the accomplishment of the settlor's purposes in disposing of his own property the trustee will quite properly be influenced by the wishes of the settlor in exercising with him an absolute power of revocation. Under these circumstances the exercise of a power to revoke does not cut off interests already vested, but is merely the exercise of a right to which those interests were always subject. The reserved right of revocation is superior to every right of the beneficiary and when exercised by the grantor with the trustee's consent restores to the settlor the full enjoyment of his property terminating all interest of the beneficiary therein.

We do not believe that in deciding *Corliss* v. *Bowers, supra,* this Court meant to lay down a rule that Congress could tax trust income to the settlor only if he had the unqualified power to appropriate the income to his own benefit and not otherwise. Such a holding would seem from a practical standpoint to be inconsistent with the decisions in *Lucas* v. *Earl,* 281 U. S. 111, and *Burnet* v. *Leininger,* 285 U. S. 136, where it was held that

an assignor was taxable upon income he had no right to use for his own purposes. In any event, whether a grantor has sufficient "unfettered command" of income, of which this Court spoke in the *Corliss case* (p. 378), to warrant his being taxed upon the income, would seem logically to be less a problem of technicalities than of actualities. Congress was justified in assuming that a power of revocation inserted in a trust instrument was inserted for a real purpose, and that the purpose was the same whether the power could be exercised by the grantor alone or by him and another whom he has chosen to act with him. Where a settlor thus makes clear his intention to retain command it may reasonably be assumed that nothing will be done in sharing command which will defeat the settlor's purpose to revoke the trust whenever he wishes. Certainly it can hardly be thought that the grantor, in selecting the person who is to share with him "unfettered command" will choose one who may not be trusted to carry out his wishes. The statute should not be tested by inquiring in each case whether amenability exists, as was suggested in *Commissioner* v. *McCormick,* 43 F. (2d) 277, 279 (C. C. A. 7th), reversed, 283 U. S. 784. But if the Constitution prevents Congress from adopting the reasonable view that the grantor has retained practical control in all situations where the consent of a person holding an adverse interest is not required, then the taxing power may be circumvented by the simple expedient of introducing

a straw man, who, in the eyes of the law, assumes a substance he does not possess. The Constitution does not require Congress to close its eyes to things which are obvious to everyone else in this practical world. The grantor in this case might have limited exercise of the power of revocation by requiring consent of one or more of his children, but they were all beneficiaries and had their own interests to consider. He did not do so. Instead he chose another, one in whose corporate judgment he presumably had confidence. That this trustee could be expected to respect the grantor's wishes is demonstrated, were demonstration necessary, by the fact that the wife's trust was subsequently modified with this trustee's consent to her definite financial loss. (R. 59.) We submit that it is not capricious to assume that a settlor who avoids an adverse interest in choosing a party to share his power has selected a friendly one. The two jointly command for the benefit of the one, and it seems not unreasonable that Congress should provide that that one should bear the burden. The same conclusion should be reached here that was reached in *Corliss* v. *Bowers, supra.*

This result is also supported by several of this Court's decisions with respect to taxes upon estates and inheritances and upon gifts. Had the grantor in this case died while the Revenue Act of 1924 was in force and before October 22, 1924, the date when the power of revocation was canceled, the value of the trust property would have been taxable as a

part of his gross estate under Section 302 (d) of the Revenue Act of 1924, and this tax, we submit, would have been constitutional.

In *Wells* v. *Commissioner,* decided February 4, 1933 (C. C. A. 8th), the court said:

> The relation that must exist between the taxpayer and the income for which he is taxable should be no different than the relation which must exist between a decedent and the property by which a transfer or succession tax is to be measured * * *. If the trust property may not be made a part of petitioner's estate at death it is difficult to understand how the income therefrom may be part of his income during life.

Conversely, if the corpus of a trust may be included in the settlor's estate at death, taxation of the income to him during life can not be said to be an abuse of the taxing power. This Court said in *Burnet* v. *Guggenheim,* No. 283, October Term, 1932, decided February 6, 1933, that—

> If * * * a power to revoke does not postpone for the purpose of taxation the consummation of the gift, then the income of these trusts is exempt from the tax as fully as the principal. What passed to the beneficiaries was the same in either case, an interest inchoate and contingent till rendered absolute and consummate through receipt or accrual before the act of revocation.

In *Saltonstall* v. *Saltonstall,* 276 U. S. 260, the grantor of a trust had the power, acting jointly

with a trustee, to alter or revoke the trust. This Court held that it was not a violation of the Fourteenth Amendment for a State to impose a tax on the succession to the corpus at the occasion of the grantor's death. We believe it unimportant that the tax there involved was a succession tax and not a transfer tax. Transfer and succession are but counterparts—two facets of the same die. If succession is not complete until death, there is no completed transfer before that time, and if the transfer is complete the succession of necessity must be complete. Cf. *Porter* v. *Commissioner,* 60 F. (2d) 673 (C. C. A. 2d), No. 466, October Term, 1932. The decision in the *Saltonstall case,* we believe, is a direct and conclusive authority in support of our position here.

Another decision tending to show that the trust property in this case could validly have been included in the settlor's gross estate is *Tyler* v. *United States,* 281 U. S. 497, where this Court upheld a transfer tax at the death of a tenant by the entirety measured by the value of the whole tenancy. There, as here, the decedent could not alone dispose of the property during his life; such action required the concurrence of another, and in the *Tyler case* that other had a substantial adverse interest. Here the one whose concurrence was required had no adverse beneficial interest. The decedent's power of disposition in this case was therefore at least as great as that of the tenant in the

Tyler case. See also *Chase National Bank* v. *United States,* 278 U. S. 327; *Reinecke* v. *Northern Trust Co.,* 278 U. S. 339; *Philips* v. *Dime Safe D. & T. Co.,* 284 U. S. 160; *Gwinn* v. *Burnet,* 287 U. S. ——, decided December 5, 1932; *Third National Bank & Trust Co.* v. *White,* 287 U. S. ——, decided December 19, 1932.

If, as these cases seem to show, it would have been neither arbitrary nor capricious for Congress to have included the corpus of the trusts in question in the grantor's estate had he died prior to October 22, 1924, it would seem equally clear that it is neither arbitrary nor capricious for Congress to impose upon the grantor during his life a tax based upon the income of those trusts. Anything to the contrary in cases like *Farmers' Loan & Trust Co.* v. *Bowers,* 29 F. (2d) 14 (C. C. A. 2d), *White* v. *Erskine,* 47 F. (2d) 1014 (C. C. A. 1st), or *Stewart* v. *Commissioner,* B. T. A., decided January 31, 1933, must, so far as applicable to the present situation, be regarded as not authoritative, in the light of this Court's decisions in the *Saltonstall* and *Tyler cases.*

There are other considerations which we believe give further support to the view that the tax in question is not an abuse of power on the part of Congress. It is well settled that a person may not escape liability for tax upon income by assigning it to another, even if the assignment is in terms in advance of production of the income, unless he ir-

revocably and unqualifiedly gives him as well the property which produces it. *Burnet* v. *Leininger,* 285 U. S. 136; *Lucas* v. *Earl,* 281 U. S. 111; *Bing* v. *Bowers,* 26 F. (2d) 1017 (C. C. A. 2d), affirming 22 F. (2d) 450 (S. D. N. Y.); *Mitchel* v. *Bowers,* 15 F. (2d) 287 (C. C. A. 2d), certiorari denied, 273 U. S. 759; *Nelson* v. *Ferguson,* 56 F. (2d) 121, 124 (C. C. A. 3d), certiorari denied, 286 U. S. 565; *Parker* v. *Routzahn,* 56 F. (2d) 730 (C. C. A. 6th); *Dickey* v. *Burnet,* 56 F. (2d) 917, 920 (C. C. A. 8th), certiorari denied October 10, 1932; *Van Meter* v. *Commissioner,* 61 F. (2d) 817, 818–819 (C. C. A. 8th); *Ward* v. *Commissioner,* 58 F. (2d) 757 (C. C. A. 9th); *Leydig* v. *Commissioner,* 43 F. (2d) 494, 496 (C. C. A. 10th); *Porter* v. *United States,* 52 F. (2d) 1056, 1057 (C. Cls.). As said in the *Parker case, supra* (p. 733), for an assignor to rid himself of liability for income tax he must make "an irrevocable assignment, not merely of future income but of the property from which such income afterwards arises." If this is true in case of an assignment, it is obvious that from a practical standpoint there is no good reason why a different requirement should apply to a trust arrangement. Unless the donor gives him the property too, the donee in substance gets no more in the one case than in the other. In the last analysis the gift is only of the income in either situation.

One of the specific reasons which moved Congress to enact Section 219 (g) was the elimination

of this manifest unfairness. The Senate Committee on Finance said in respect of the statute (Senate Report No. 398, 68th Cong., 1st Sess., p. 25):

> The creation of a revocable trust constitutes nothing but an assignment of the right to receive future income. Since such an assignment does not operate to increase[3] the taxable income of the assignor, the creation of a revocable trust should not so operate, but the income of such a trust should be included in the income of the grantor. The bill so provides.

Congress thought that it was only fair that one who gives to another, through a trust arrangement, the income of property which he has the power either then or later to repossess, acting either alone or in conjunction with another whom he has chosen to share his power with him, should be taxed upon that income just as a person is taxed upon income he gives to another by means of an assignment, either for a definite period or for so long as the assignor may be so inclined. It intended by Section 219 (g) to establish that policy and that, we submit, should be sufficient to sustain the petitioner's position.

It is no answer to say that in situations like that in the *Leininger case* the donor accomplishes his purpose by retaining legal title to the corpus which produces the income, for here the settlor was one

[3] The word "increase" is manifestly an error for "decrease."

of the trustees and shared the legal title. Obviously, the donor has no greater beneficial rights in the income when he retains the legal title than when, for reasons of his own, he makes trustees the channel of title. In essence there is no difference. For practical purposes the donee gets no more in the one situation than in the other, and taxation, it has many times been said by this Court, is a practical matter, attaching little importance to the technical refinements of title which a taxpayer may employ to reach his ends. *Tyler* v. *United States, supra,* p. 503; *Burnet* v. *Guggenheim,* No. 283, October Term, 1932, decided February 6, 1933. In cases of this kind it cares less for the vehicle a donor may use to serve his purpose than for what he accomplishes by its use. It was said in *Weiss* v. *Stearn,* 265 U. S. 242, 254, that "when applying the provisions of the Sixteenth Amendment and income laws enacted thereunder we must regard matters of substance and not mere form." Putting aside the form, it is obvious that the beneficiaries in the case at bar got no more than the assignee in the *Leininger case;* both got income and income alone, and if it is reasonable to tax the donor of the income in the one situation, it should be reasonable to do so in the other.

Unlike *Hoeper* v. *Tax Commission,* 284 U. S. 206, upon which the respondents relied below, the present case is not one where one person is taxed for income derived by another from his own separate

property. In the *Hoeper case* the income which the State sought to tax to the husband was earned by the wife's own efforts or was the fruit of property which she owned in her own right and with which neither her husband nor anyone else had any connection and over which he could exercise no rights. Quite different is the situation here. In this case the beneficiaries had no power to pledge, sell, or bequeath the property. The grantor and one of the two trustees had all the rights and powers incident to absolute ownership of the property. Between them they had what was the equivalent of a fee. *Bullen* v. *Wisconsin*, 240 U. S. 625, 631. It lay in their power to control or dispose of the corpus without consulting the beneficiaries. The latter were not, like the wife in the *Hoeper case*, the owners of the property which produced the income. Cf. *Burnet* v. *Guggenheim, supra; Porter* v. *Commissioner*, 60 F. (2d) 673 (C. C. A. 2d), now pending before this Court on certiorari, No. 466, October Term, 1932.

Congress had in mind still another purpose in enacting Section 219 (g). That purpose was "to secure clarity and to prevent the evasion of taxes by means of estates and trusts."[4] House Report No.

[4] So far as they have spoken on the point, the courts have said that Section 219 (g) did not operate to change the law but was merely declaratory. *McCauley* v. *Commissioner*, 44 F. (2d) 919, 920 (C. C. A. 5th); *Dickey* v. *Burnet*, 56 F. (2d) 917, 920 (C. C. A. 8th), certiorari denied October 10, 1932, *supra*. The statement of the committees that the purpose of this section was "to secure clarity" supports this view.

179, 68th Cong., 1st Sess., p. 21; Senate Report No. 398, *supra*, p. 25; *Corliss* v. *Bowers*, 34 F. (2d) 656, 657–658 (C. C. A. 2d), affirmed, 281 U. S. 376. The statute was designed to correct an existing evil. This fact was deemed important in the *Tyler case, supra*. It is no less so here. In this case in respect of income taxes, as in that case in respect of estate taxes (p. 505), "the evident and legitimate aim of Congress was to prevent an avoidance"; and here as there, "the provision under review is an adjunct of the general scheme of taxation of which it is a part, entirely appropriate as a means to that end. *Taft* v. *Bowers*, 278 U. S. 470, 482."[5]

The facts in *Bromley* v. *Commissioner*, 26 B. T. A. 878, now pending in the Circuit Court of Appeals for the Third Circuit, present a situation closely analogous to that here involved. Each of four brothers created a trust in 1921 for the bene-

[5] Unless the income involved in this case is taxed to the settlor, it seems very likely that so much of it as was distributable to the beneficiaries will go untaxed. Each installment of income from a revocable trust is a gift to the beneficiary. I. T. 2145, IV–1, Cumulative Bulletin 43; Regulations 67, Art. 1; see *Burnet* v. *Guggenheim*, *supra*. The amounts received by the beneficiaries would not be taxable as income to them, for gifts are not subject to the income tax. See Section 213 (b) (3) of the Revenue Act of 1924. The income which was distributable to the beneficiaries would not be taxable to the trustee. Section 219 (b) (2) of the Revenue Act of 1924.

fit of his children. The four brothers were trustees of each trust and each trust could be revoked only with the consent of all the trustees. The Board of Tax Appeals held that the income of each trust was taxable to the grantor under Section 219 (g) and that the statute was not invalid. It said (p. 880):

> The purpose of the statute here involved, as disclosed by reports of Congressional Committees, is to prevent evasion of tax by means of trusts. * * * To effect this end, Congress enacted that where the creator of a trust reserves the right of revesting the property in himself—acting either alone or in conjunction with anyone not a beneficiary—the income shall be considered to be his income. We see nothing unreasonable in this when its purpose is considered. "If the taxation involves reasonableness to meet the desired ends of fair play, it is valid." *Corliss* v. *Bowers,* 34 F. (2d) 656.

III

THE STATUTE DOES NOT HAVE AN INVALID RETROACTIVE OPERATION

The respondents urged below (Br. 26–28), and it was upon this point that the Circuit Court of Appeals decided the case (R. 96), that since the trusts in question were created before the enactment of Section 219 (g), enforcement of the stat-

ute would be contrary to the Fifth Amendment, because of what is said to be its retroactive operation. We submit that this position is without merit.

In support of their contention the respondents relied upon decisions dealing with the constitutional limitations upon the authority of Congress to impose death duties and gift taxes. The distinction between those situations and the one here in question would seem to be obvious. Cases like *Nichols* v. *Coolidge,* 274 U. S. 531, *Untermyer* v. *Anderson,* 276 U. S. 440, and *Blodgett* v. *Holden,* 275 U. S. 142, turn upon the power of Congress to tax transfers or gifts made and completed before the laws assuming to tax them were enacted. Such impositions this Court held were arbitrary and invalid. But here there is no attempt to tax the creation of the trusts or the transfer of the securities to the trustees, but only the income received from the trust property. That income arose after January 1, 1924, the effective date of the law (Section 283 of the Revenue Act of 1924 (*infra,* p. 28)), and although the Revenue Act of 1924 was not enacted until June 2, 1924, such limited retroactivity is common in income tax laws and has uniformly been sustained as lawful. See *United States* v. *Cooper,* 280 U. S. 409, 411. Cf. Revenue Act of 1918, enacted on February 24, 1919, but applicable to 1918 income; *Fawcus Machine Co.* v. *United*

States, 282 U. S. 375, 379. Certainly there is no retroactivity as to the income arising after June 2, 1924, the date the Revenue Act of 1924 was enacted. And as to the income arising in 1924 before June 2, 1924, the question seems indistinguishable from that in *Corliss* v. *Bowers,* 281 U. S. 376, where the trust involved, like the trusts here in issue, was created in 1922. That portion of the income had passed as completely beyond the settlor's control, when the Revenue Act of 1924 was enacted, in the *Corliss case* as in this. The statute was sustained, although the taxpayer contended that it was invalid on account of retroactivity.

A person has no vested right against taxation of future income. The Sixteenth Amendment did not give Congress the power to impose income taxes. That power already existed; the Amendment merely removed the requirement of apportionment. *Brushaber* v. *Union Pac. R. R. Co.,* 240 U. S. 1. Nevertheless, despite all the other constitutional provisions, it is clear that upon its adoption Congress could tax without apportionment "everything that became income, in the ordinary sense of the word, after the adoption of the Amendment" (*Lynch* v. *Hornby,* 247 U. S. 339, 343–344), whether the particular source came into being before or after that time. And so here Congress could tax the income arising after the effective date of Section 219 (g) though the trusts were created in 1922.

CONCLUSION

The judgment of the Circuit Court of Appeals should be reversed.

Respectfully submitted.

THOMAS D. THACHER,
Solicitor General.
SEWALL KEY,
HAYNER N. LARSON,
Special Assistants to the Attorney General.
ERWIN N. GRISWOLD,
Attorney.

MARCH, 1933.

APPENDIX

STATUTES INVOLVED

The Revenue Act of 1924, c. 234, 43 Stat. 253, 277, 303, 304, contained the following provisions:

SEC. 219. * * *

(g) Where the grantor of a trust has, at any time during the taxable year, either alone or in conjunction with any person not a beneficiary of the trust, the power to revest in himself title to any part of the corpus of the trust, then the income of such part of the trust for such taxable year shall be included in computing the net income of the grantor.

(h) Where any part of the income of a trust may, in the discretion of the grantor of the trust, either alone or in conjunction with any person not a beneficiary of the trust, be distributed to the grantor or be held or accumulated for future distribution to him, or where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor (except policies of insurance irrevocably payable for the purposes and in the manner specified in paragraph (10) of subdivision (a) of section 214), such part of the income of the trust shall be included in computing the net income of the grantor. (U. S. C., Title 26, Section 960.)

* * * * *

SEC. 283. This title shall take ffect as of January 1, 1924.

* * * * *

SEC. 302. * * *

(d) To the extent of any interest therein of which the decedent has at any time made a transfer, or with respect to which he has at any time created a trust, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke, or where the decedent relinquished any such power in contemplation of his death, except in case of a bona fide sale for a fair consideration in money or money's worth * * * (U. S. C., Title 26, Sec. 1094.)

U. S. GOVERNMENT PRINTING OFFICE: 1933